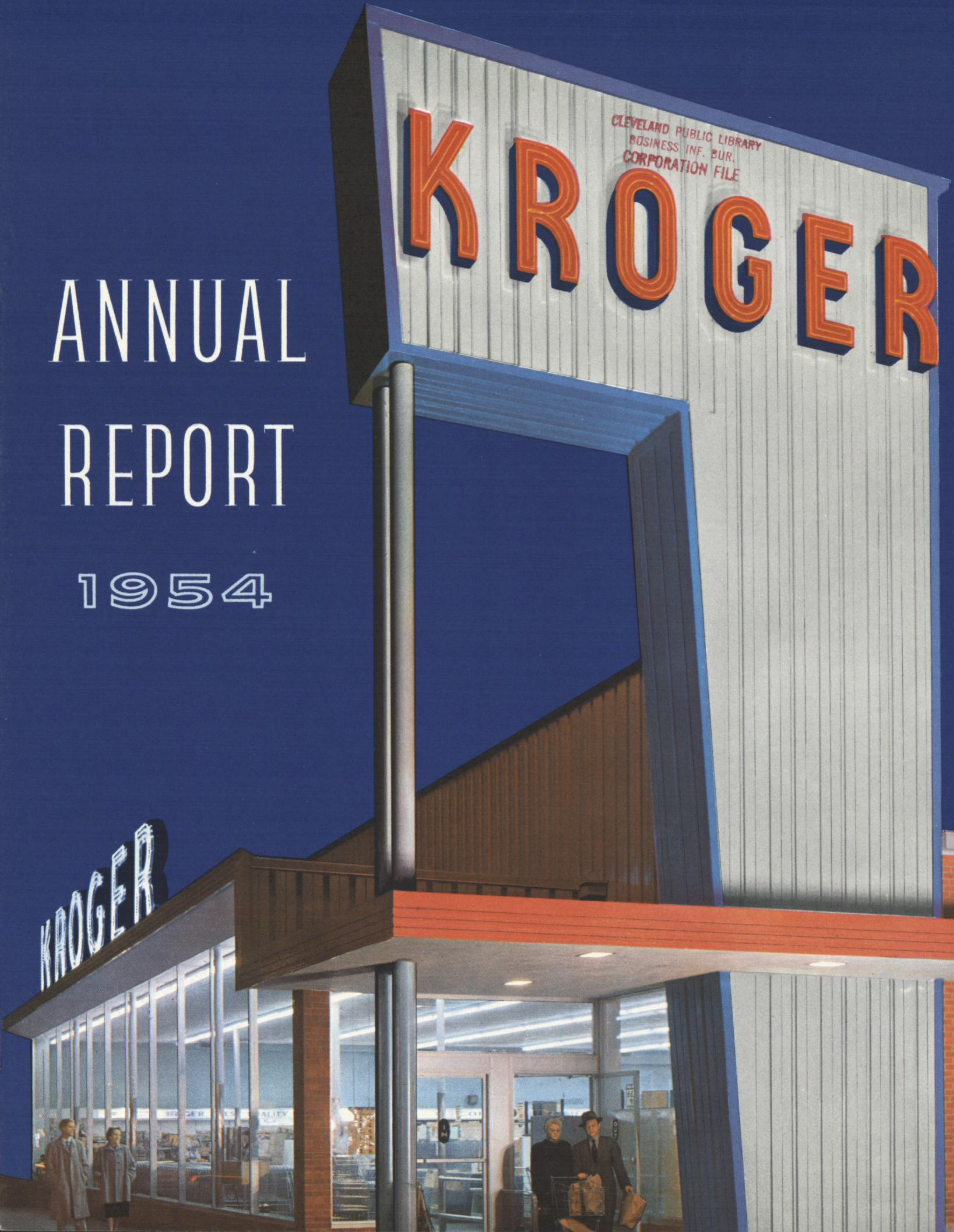
ANNUAL REPORT

1954



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President's Letter

Sales of $1,108,694,168 for 1954 (53 weeks) reached a new high, exceeding 1953 (52 weeks) by $50,085,517 or 4.7%. A normal Kroger year consists of thirteen four-week periods, a total of 52 weeks or 364 days. Every sixth year, an extra week is included in the business year to correct our calendar. 1954 was such a year. For the comparable 52 weeks, our sales gain was 3.0%, all of which was due to increased tonnage.

The Kroger Co. earned $14,912,912 in 1954, equal to $4.04 per share. Net income in 1953 was $3.40 per share. These figures are not directly comparable because of a change in leasehold accounting. Excluding charges for leasehold improvements in both years, net income for 1954 exceeded that of 1953 by $0.04 per share.

Since 1932 it had been Kroger's policy to write off leasehold improvements as they were acquired, even though these assets had a normal useable life of about five years. Although the impact of these charges varied with our store construction program, it has been only in recent years that the amounts involved have been sufficient to materially affect reported results.

In 1954 it was decided to adopt the accounting method that amortizes leasehold improvements over their useful life. This method, which is generally used in the retail food industry, has been required by the Treasury Department for income tax purposes. The revised accounting policy will more accurately report both assets and earnings.

Operating and general expenses increased $8,938,776 or 6.0%. Salaries and wages increased 8.4%. The company has availed itself of the accelerated depreciation provisions of the 1954 Internal Revenue Act and has thereby effected a reduction of $525,000 in its 1954 income tax. We will continue to use the straight-line depreciation method for reporting income to shareholders.

During the year the regular quarterly dividend was increased from $0.40 to $0.45 per share. A year-end dividend of $0.20 increased total payments for the year to $2.00, the same as in 1953.

Cash at the year-end was $34,627,962, down $7,164,757 from a year ago. The decline is due to increased outlay for capital assets and a reduction in current liabilities of $1,456,105. Net working capital was $67,522,366, a decline of $1,185,209 during the year. We consider the present working capital to be ample. Retail inventories at the year-end were $71,693,956, equal to 6.5% of sales. A year ago they were $69,350,530 or 6.6% of sales.

In 1954 capital expenditures totaled $17,966,196, as compared with $12,113,616 in 1953 and $10,227,038 in 1952. Depreciation was $6,842,257 and amortization was $340,942. Completed store properties were sold for an aggregate of $1,102,488.

Capital expenditures for stores were $11,508,024, of which $1,210,575 was for store land and buildings acquired for resale. One hundred twenty-two new or remodeled stores were opened during 1954. The total number of stores at the end of the year was 1678, a net decline during the year of 132. In 1929 Kroger operated 5575 stores, but total sales were only $286,611,215. A drastic change has occurred in size, sales volume and character of food stores over the years. Kroger still has a few small, pre-war, service-type units, but the majority are modern, self-service stores.

A typical new store opened today involves an investment by the company of $225,000 for store fixtures, equipment, leasehold improvements, inventory and related transportation and warehousing facilities. Land and buildings are normally financed and built by landlords and leased to Kroger, although in some locations it has been advantageous to purchase land, construct the building and sell the property on a lease-back basis.

Capital expenditures for warehouses and related equipment were $3,241,843. A warehouse in Wichita, Kansas, and a branch office and perishable products warehouse in Cincinnati were completed and occupied in 1954. The Louisville, Kentucky, and Toledo, Ohio, units will be completed in 1955. Plans are under way for new warehouses in Columbus, Ohio, and Little Rock, Arkansas. Studies are being made of other units which are inadequate and inefficient by today's standards. $1,537,110 was expended on transportation equipment and $356,258 on office equipment.

In 1954 we expended $1,322,961 on capital assets for our Manufacturing Division. The principal expenditure was for equipping a new bakery at Memphis, Tennessee.

Our Kroger team of 30,320 employees are working together to meet the problems of this highly competitive industry. 96% of those eligible are members of the Employees' Savings and Profit Sharing Plan. They are active in improving earnings because they share in them.

For 1954, company profits of $1,347,604 were contributed to the plan, while the employees saved and deposited $3,190,802. The fund assets at the year-end were $14,749,845, including 24,100 shares of Kroger stock. Through their stock ownership, the employees have an added incentive to improve results.

Management is increasing its participation in the company through ownership of Kroger stock under the Stock Option Plan. 24,930 shares have been purchased.

We are intensifying the management training and development program which was established several years ago. Outstanding young men are being brought into the company as management trainees. It is gratifying to see the progress they are making in the company. Many already have achieved positions of responsibility.

Walter A. Draper, Charles M. Robertson and Donald M. Wood will not be nominees for re-election as directors at the annual meeting. The company will continue to have the benefit of the advice and counsel of Mr. Draper and Mr. Robertson as directors emeritus and of Mr. Wood as a director of Manufacturers & Merchants Indemnity Company.

In his twenty-five years of active service as a director, vice-president and treasurer, president, and chairman of the board, Mr. Robertson made important contributions to the financial strength and stability of the company. As a director since 1931, Mr. Draper has shared with our company his broad business experience, and for a number of years has served as chairman of the board's audit committee. Mr. Wood's wide knowledge and understanding in the field of insurance were helpful in the development and management of the company's insurance subsidiary.

1955 will be a good year for business—but a competitive one. Consumer expenditures should reach new highs. Food sales will be good, but all companies will be striving to increase volume through new stores, special promotions, aggressive prices and better merchandising. Kroger expects to improve its position.

Respectfully submitted,

Joseph B. Hall

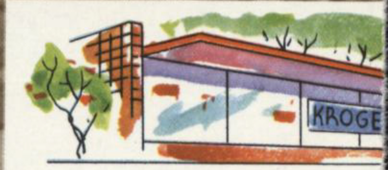
February 11, 1955

President

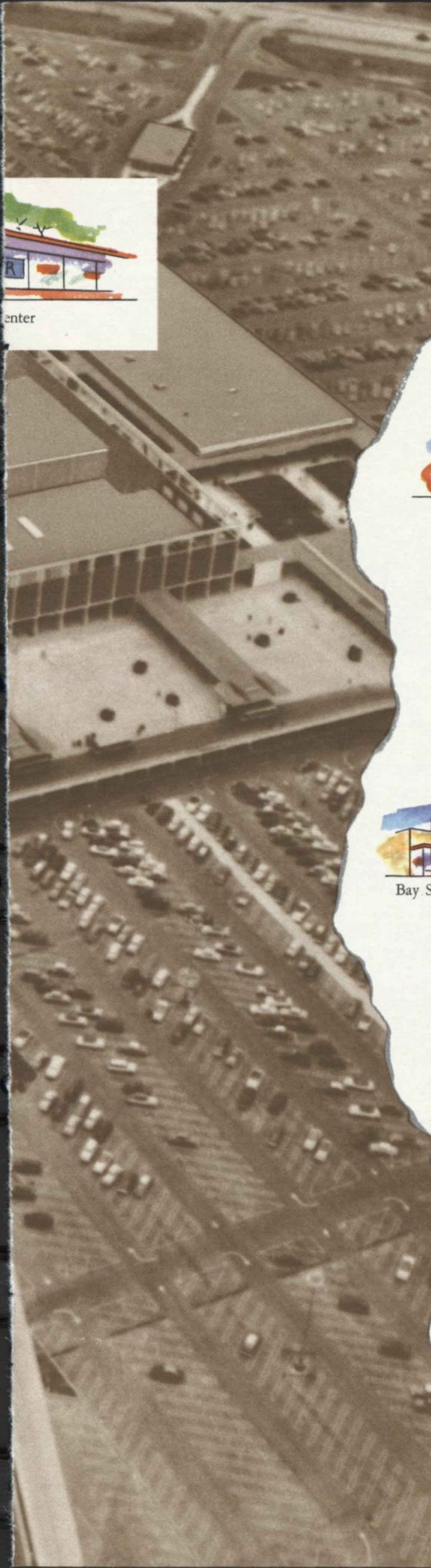
In 1954 Kroger continued its long-range program of store modernization and improvement. New stores are being built to serve areas of population growth and to render better service in areas where we already are represented. Existing stores in established locations are being remodeled to provide modern fixtures and facilities.

A number of our new stores are located in planned shopping centers. We believe that such developments, properly planned, offer advantages to our customers. The majority, however, are individual stores, located to provide a maximum of accessibility and convenience, and designed to meet the sales potential and shopping needs of the area.

Representative examples of our new stores are shown here.



Northland Shopping C
Detroit, Mich.



enter

261 N. Broad St.
Galesburg, Illinois

642 E. Lockwood
Webster Groves, Missouri

Plum & Oakhurst
Parkersburg, West Virginia

Frandor Shopping Center
Lansing, Michigan

4th & Chestnut
Pine Bluff, Arkansas

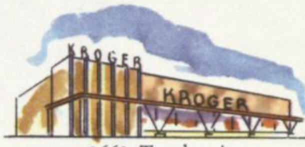
35 S. Central Ave.
Fairborn, Ohio

2003 Bankhead Hwy.
Atlanta, Georgia

Town & Country Shopping Center
Monroeville, Pa.

Graceland Shopping Center
Clinton Twp., Ohio

14010 Detroit Ave.
Lakewood, Ohio



3660 Topeka Ave.
Topeka, Kansas

Bay Shore Shopping Center
Glendale, Wis.

Cardinal Point Shopping Center
Paducah, Ky.

7545 Ten Mile Rd.
Centerline, Michigan

Patterson Ave. & N.W. Blvd.
Winston-Salem, N. C.

115 Walnut St.
Terre Haute, Indiana

E. 2nd St. & Government Place
Maysville, Ky.

201 S. Florissant
Ferguson, Missouri

2147 E. 5th Ave.
McKeesport, Pa.

Lamar-Airways Shopping Center
Memphis, Tenn.

6220 Guilford Ave.
Indianapolis, Indiana

The Kro

Consolidated Balance

Assets

Cash			$ 34,627,962
Receivables			4,177,334
Merchandise inventories (Note 1)			84,667,841
Store and general supplies			3,434,475
Prepaid insurance, rent and taxes			1,593,696
Total Current Assets			128,501,308
Investment in subsidiary insurance company, at cost (Note 2)			1,776,361
Land, at cost or less		$ 2,569,335	
Leasehold improvements, net		3,415,090	
Buildings, at cost or less	$17,194,385		
Machinery and equipment, at cost	79,257,870		
	96,452,255		
Less allowance for depreciation	42,861,545	53,590,710	
Net Fixed Assets			59,575,135
Total Assets			$189,852,804

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Sheet—January 1, 1955

LIABILITIES

Accounts payable			$ 30,440,148
Accrued expenses			14,848,657
Provision for federal taxes			15,690,137
TOTAL CURRENT LIABILITIES			60,978,942
Long-term notes (Note 3)			14,000,000
Employees' benefit fund			2,288,658

CAPITAL

Preferred capital stock, par $100:			
First preferred, 6%, 279 shares outstanding	$27,900		
Second preferred, 7%, 150 shares outstanding	15,000	$ 42,900	
Common capital stock, without par value (Note 4):			
Authorized 5,000,000 shares			
Outstanding 3,693,839 shares		34,341,402	
Accumulated earnings (Note 3)		78,200,902	112,585,204
TOTAL LIABILITIES & CAPITAL			$189,852,804

Consolidated Statement of Income

Years Ended January 1, 1955 and December 26, 1953

	1954	1953
Sales	$1,108,694,168	$1,058,608,651
Cost of sales	923,625,793	880,496,300
Operating and general expenses	157,741,463	148,802,687
Total	1,081,367,256	1,029,298,987
Income before federal taxes on income	27,326,912	29,309,664
Federal taxes on income	12,414,000	16,781,000
Net income	$ 14,912,912	$ 12,528,664

Consolidated Statement of Accumulated Earnings

Year Ended January 1, 1955

Accumulated earnings—December 26, 1953		$70,670,362
Total net income for 1954	$14,912,912	
Dividends declared in 1954	7,382,372	7,530,540
Accumulated earnings—January 1, 1955		$78,200,902

Notes to Financial Statements

1. Merchandise inventories are valued in part on the LIFO basis and in part at the lower of cost or market.
2. The investment in Manufacturers & Merchants Indemnity Company, an insurance company licensed under the laws of the State of Ohio, represents the entire preferred stock and 66⅔% of the common capital stock of that company, and is carried on the books at cost. At January 1, 1955, the company's equity in the net assets of the insurance company determined in accordance with the rules of the Commissioner of Insurance of the State of Ohio, amounted to $1,477,232. Total assets of the insurance company, so determined amounted to $6,954,296 consisting principally of cash, U. S. Government securities and other marketable securities aggregating $6,464,427. Operations of the insurance company for the year 1954 resulted in an increase in surplus of $148,670.
3. Notes bearing interest at 3.1% mature October 1, 1971. Annual prepayments of $700,000 without premium, are required beginning October 1, 1961. Any of the notes may be prepaid at the option of the company at premiums provided in the loan agreement. Payments of cash dividends are limited to earnings subsequent to January 1, 1955, plus $36,105,902 of accumulated earnings existing on that date.
4. Options granted to 314 officers and executives for the purchase of 153,189 shares of Kroger common stock were in force at January 1, 1955. The option price of 111,246 shares was $32.25. Option prices of the balance of 41,943 shares ranged from $33.25 to $39.25. Options for 13,591 shares were exercisable at January 1, 1955. Options for 12,560 shares were exercised during 1954 at prices ranging from $32.25 to $38.25.
5. See Page 1, President's Letter, regarding change in accounting for leasehold improvements.

Report of Certified Public Accountants

To The Board of Directors,
The Kroger Co.
Cincinnati, Ohio

We have examined the consolidated balance sheet of The Kroger Co. and subsidiary company as of January 1, 1955, and the related consolidated statements of income and accumulated earnings for the fiscal year (fifty-three weeks) then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated balance sheet and statements of income and accumulated earnings present fairly the consolidated financial position of The Kroger Co. and subsidiary company at January 1, 1955, and the results of their operations for the fiscal year then ended, in conformity with generally accepted accounting principles applied on a basis consistent (except for the change in accounting for leasehold improvements, as discussed on page 1 of the President's Letter, with which change we concur) with that of the preceding fiscal year.

Lybrand, Ross Bros. & Montgomery
Certified Public Accountants

Cincinnati, Ohio
February 11, 1955

Financial and Operating Statistics

	1954	1953	1952	1951	1944
SALES	$1,108,694,168	$1,058,608,651	$1,051,849,935	$997,086,223	$455,438,169
NET INCOME BEFORE TAXES	$ 27,326,912*	$ 29,309,664	$ 27,935,387	$ 25,255,540	$ 14,909,599
NET INCOME	14,912,912*	12,528,664	12,110,087	12,657,940	5,144,399
NET INCOME PER SHARE	$4.04*	$3.40	$3.30	$3.45	$1.40
DIVIDENDS PER SHARE	$2.00	$2.00	$1.90	$1.85	$1.00
NUMBER OF SHAREHOLDERS	25,501	25,914	26,088	26,254	27,194
NUMBER OF STORES	1,678	1,810	1,891	1,978	2,896
NUMBER OF EMPLOYEES	30,320	29,105	28,396	26,864	18,425
CASH	$ 34,627,962	$ 41,792,719	$ 40,078,625	$ 30,128,288	$ 29,495,550
MERCHANDISE INVENTORIES	84,667,841	81,196,446	77,143,349	79,170,757	38,052,582
NET WORKING CAPITAL	67,522,366	68,707,575	65,884,745	61,528,850	47,680,902
NET FIXED ASSETS	59,575,135	50,451,043	47,843,817	47,087,347	14,825,859
ACCUMULATED EARNINGS	$ 78,200,902	$ 70,670,362	$ 65,501,630	$ 60,373,344	$ 19,849,724
NET WORTH	112,585,204	104,646,321	99,216,265	94,090,179	53,617,859
NET WORTH PER SHARE	$30.47	$28.41	$27.00	$25.60	$14.57

*Reflects change in leasehold improvement accounting.

Kroger

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